



February 20, 1998

[Bonneville Power Administration Cost Review Panel](#)

c/o [Northwest Power Planning Council](#)

851 SW Sixth Avenue, Suite 1100
Portland, OR 97204

SUBJECT: Comments on Bonneville Cost Review Draft Recommendations

Dear Cost Review Panel:

I am writing to convey the perspective of the Washington State Department of Community, Trade and Economic Development (CTED) on your recommendations for cuts in the operating costs of the Bonneville Power Administration.

We would like to commend you for the thorough work that you did in a short amount of time. Your management insights have produced a draft report that has the potential to lead to long-overdue reforms, most of which would substantially reduce costs without compromising achievement of Bonneville's policy objectives. While we take issue with some of your recommendations, we appreciate the zeal with which you approached your goal of ensuring that BPA remains competitive and thus in a position to continue to provide public benefits to the Pacific Northwest.

Our comments are organized as follows. We have some general observations about the *Draft Recommendations* followed by detailed comments about each recommendation.

General Comments on the Draft Report as a Whole

As a general matter we support all of the management recommendations, but we have grave concerns in the areas where the Cost Review strayed into policy. We see the Cost Review as an extraordinary opportunity to cleanly separate management issues from policy issues, so as to focus on the former without invoking the controversies associated with the latter. With the policy issues put aside, we hoped and expected that this group could take a sharp- pencilled look at costs without the necessity for the kind of time-consuming, representative forum that policy deliberations require. This Committee was selected exclusively for its management expertise and that expertise is evident in the management

recommendations. In your final report, you can retain virtually everything that improves BPA's financial bottom line without compromising its bottom line policy objectives.

The proposed reductions in BPA's and the Power Council's stewardship functions imply a view of the future that assumes a few years of intense change and adaptation followed by, after 2001, a period of relative calm. This is very unlikely. As the electricity industry becomes more dynamic due to increasing competitive forces, BPA will continue to adapt in ways that we cannot foresee. Similarly, the political and policy oversight of BPA's role in the region will remain complex. With federal and state changes in the electric industry, the role of utilities will change and new actors will emerge in both the generating and marketing of electricity. Distributed generation will increase, upsetting all of our settled ideas about electric supply, pricing and transmission. The region as well as the individual states will need both the analytic and political capabilities of the Northwest Power Planning Council to enable us to deal with these changes.

The goals of the Regional Act remain as compelling today as when they were written. The Act's mechanisms for achieving those goals, however, are largely outmoded. Because we remain committed to those goals, we believe that the Council's analytical and leadership roles are at least as important (though less well defined) today as they were in 1980. The exact nature of those roles is worth reviewing, but again, not in the context of a policy-neutral cost-cutting exercise.

Stripped of the Council's oversight and its own stewardship functions, BPA could suffer many of the same accountability and political problems that plague TVA. Because of the Act, the Council, and BPA's own stewardship efforts BPA has become more responsive to the region and more receptive to the kind of scrutiny the Cost Review exemplifies. We believe that this kind of strong, mutually accountable state-federal partnership in the management of the Columbia River System is essential.

Specific Comments on Individual Recommendations

1. Reductions in Power Business Line Staffing

We agree with the underlying assumptions regarding this recommendation, but as with the recommendations to reduce BPA overhead (#8) some caution is in order. Clearly, if BPA's rates are below market, BPA can play a more passive role in the market place. However, there are risks to being the only passive wholesale seller of electricity in a very dynamic market. In reducing its marketing staff, BPA will need to make sure it can still respond to unexpected changes in the market and to the needs of its customers. BPA should also retain the ability to maximize the value of its products, consistent with preference. This ability increases the value of its firm power products to preference customers.

2. Elimination of Funding for market transformation

This recommendation clearly crosses the line into policy, especially when coupled with the

suggestion that BPA's statutory obligations to promote energy efficiency be repealed. It also explicitly contravenes an important part of the Comprehensive Review's recommendations, which we believe are outside the scope of the Cost Review.

The policy rationale for BPA's continued support of energy efficiency market transformation is very strong. However, we will not explore that rationale here, as we believe that policy debates are outside the scope of this exercise. It is, however, relevant to this effort to note that this recommendation, if implemented in full, would not improve BPA's competitive position. If, as you propose, state law picks up the market transformation funding, then eliminating it from BPA's rates won't make BPA more competitive with respect to its Northwest customers. Those customers would contribute to market transformation whether they buy power from BPA or not, and would be credited against the state obligation if their BPA purchases already cover that obligation. Policy considerations aside, this recommendation contributes nothing to this Committee's goal of improving BPA's position in the Northwest market.

3. Reduce funding of legacy contracts

We note that BPA has no control over whether these contracts will be fully implemented. A possible exception is low-income weatherization contracts, where senior management has already indicated its commitment to extend the period of time (before 2001) in which the agreed-upon contract amount can be spent. Contractors have already adjusted their implementation schedules accordingly. We question whether the financial value of renegeing on these commitments would exceed the cost of lost credibility and broken agreements.

Here again, this recommendation implies a change in policy on BPA's part. We believe there are strong arguments for a continued BPA role in conservation, but we will reserve them for appropriate policy forums.

4. Further reduce funding for the NW Power Planning Council

This recommendation, though small in financial impact, is large in policy implications. We believe that policy issues of this sort require deliberations that would distract the cost review from its appropriate and much more financially significant subjects. Reconfiguring the Council to one member per state would clearly require sensitive deliberations (and legal changes), especially in Washington. We reiterate our belief that the region will continue to need a policy body to analyze the economic and political impacts of industry changes on BPA and the region and recommend policy changes to BPA, the states and to Congress.

5. Reduce planned expenditures for renewable resource projects

We see policy merit in BPA continuing its commitment to renewables, but, again, we will not address the policy rationale here. The Comprehensive Review affirmed that BPA can and should

play a useful role in stimulating the growth of renewables in the Northwest by developing resources requested by its customers and by partnering with other renewable resource developers. BPA has already started to respond to customer demand by providing a "renewable product" which reflects the desire of many distribution utilities to offer renewable power to their customers. Insofar as the incremental costs of these investments are recovered from sales of premium renewable products, we see no net cost savings in this recommendation.

6. Consolidated, integrated capital/asset management strategy for federal hydro system

This recommendation represents an enormous step forward toward creative management strategies to substantially increase the operational and financial efficiency of the FCRPS. The Corps' expertise in achieving its multiple missions needs to be respected, but it makes no sense to continue the longstanding practice of simply accepting each federal agency's independent management strategies. Integrated management of the federal system a must, and we applaud the Committee for focusing intently on this issue.

7. Market oriented strategy for WNP-2

We also agree with the recommendation to allow WNP 2 to compete on its own merits. The strategy is creative and should satisfy those, like Congressmen DeFazio, who simply want to shut it down now, and those who think that too much has been invested to walk away from it. The management and employees of the Supply System are competent and have proven themselves able to reduce costs and improve reliability. Since substantial costs will be incurred regardless of whether the plant runs or not, allowing the management and employees to give it their best shot seems appropriate.

8. Further reduce corporate overhead costs

We agree that there are many opportunities for BPA to cut its administrative and liaison costs, but we would be cautious in expecting BPA to cut 50 percent of its business services, corporate planning, public affairs and legal services costs. Even in carrying out a relatively passive and narrow power marketing role, BPA's size, market influence and responsibilities in managing a very large share of regional transmission and generation will still leave it with large planning and inter-governmental responsibilities. As we mention above, the prospect of a short period of intense change followed by a long, placid era sounds attractive, but we wouldn't count on it. Even with the full implementation of all of the recommendations of the Comprehensive Review and the BPA Cost Review, the electricity industry will be ever more dynamic as market forces take hold. BPA will still need to interact with governments at all levels, deal with complex new legal issues, and participate in regional planning activities. BPA can certainly reduce its internal and external communications functions, but perhaps not to the extent envisioned.

Finally, much of the proposed cost reductions are expected to come from the full implementation

of the new Enterprise software system. Since massive software changes are always fraught with unexpected difficulties, both the Cost Review committee and BPA should be cautious about counting on the savings that are expected from it.

9. Legislative changes in the areas of personnel management and procurement

These recommendations seem reasonable, especially reform in procurement. The State of Washington has a flexible, market-oriented procurement system that enables it to carry out its governmental functions at the lowest possible costs while maintaining public accountability. While the federal government has made some progress in this area under its reinvention initiatives, much needs to be done. Personnel and procurement reforms do not necessarily mean adopting a "business model," but simply eliminating obstacles to efficiency while maintaining public accountability.

10/11. Transmission cost functionalization

While this recommendation shifts costs rather than reducing them, it is probably worth pursuing. There may be different interpretations of whether FERC is likely to allow costs such as generation-integration into transmission rates. Our view is that to the extent that these costs have been ascribable to transmission by other generating utilities, BPA should certainly pursue the change.

12. Further reduce federal and non-federal debt service

We agree with this recommendation.

Concluding Comments

In a number of areas above, we have suggested that the proposed cuts raise policy issues that detract from the Committee's draft recommendations by straying outside the scope of a management exercise. In at least one case - market transformation - the issue was clearly raised and resolved in as broad a policy forum as we can hope for - the Comprehensive Review. We urge you to remove the policy recommendations, #s 2-5, from your final report and allow BPA to move quickly to implement the reductions in management costs that you have identified in your other recommendations.

However, should the Governors and the Council deem that further policy review is appropriate regarding the costs associated with renewable energy investments, conservation legacy programs, the Council itself and some of the corporate costs that allow BPA to perform its stewardship functions, we would be pleased to participate in an appropriate forum for such review. The future of the Council and BPA's broad stewardship role in the Northwest electricity system certainly are important issues but need the kind of policy and political expertise that complement the financial management expertise you brought to the rest of your recommendations.

Thank you for the opportunity to comment.

Sincerely,

K.C. Golden
Assistant Director